No. 89-748

IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

SECURITIES INDUSTRY ASSOCIATION,

Petitioner,

—v.—

ROBERT L. CLARKE, OFFICE OF THE COMPTROLLER OF THE CURRENCY, and SECURITY PACIFIC NATIONAL BANK,

Respondents.

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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As significant for what they omit as for what they include, respondents' briefs confirm that the requested Writ of Certiorari should issue.

1. Respondents do not even attempt to answer the fundamental inconsistency of the ruling below: If, as the Second Circuit held, Glass-Steagall does not restrict any activity the Comptroller determines to be part of the "business of banking," it restricts *nothing*. Banks can only do what they are affirmatively authorized by statute to do; all else is forbidden. (Pet. 8.) By removing the Glass-Steagall prohibitions from any activity the Comptroller deems "convenient and useful" to banking, the analysis adopted below renders Glass-Steagall, and Congress' repeated amendments to it, surplusage—mere cautions against that which a bank may not

do in any event. The Second Circuit opinion effects a monumental change in the statutory structure.

2. Where they do attempt an answer, respondents are flatly incorrect. Ignoring the broad sweep of the ruling below, respondents assert that this case involves nothing more than the sale by a bank of mortgage loans it originates.[1] The ruling is not so limited, restricted neither to mortgages nor to loans originated by the underwriting bank. The Comptroller permitted banks to underwrite to the public "mortgage-backed or *other asset-backed*" securities representing "interests in" any asset a bank may own (62a-63a; emphasis supplied). He stressed repeatedly his current belief that a national bank has the "power to sell *any* of its lawfully acquired assets" with no Glass-Steagall restriction whatsoever on the "means" of such sales. (62a-63a; 57a; emphasis supplied.) The Second Circuit upheld this ruling, finding anything the Comptroller deemed part of the business of banking to be entirely beyond Glass-Steagall restraint. (32a.) Relying upon this ruling, banks already have launched public offerings of securities backed by credit card receivables, equipment leases, automobile loans and any number of other bank assets.[2] It is not "far flung speculation" (Sec. Pac. Br. 7) that banks may underwrite junk bonds too—the ruling authorizes that and much more. (*See* Pet. 12 & n.16.)

3. Respondents are also wrong in seeking to distinguish directly contrary Glass-Steagall interpretations by the Comptroller, the Federal Reserve Board and this Court. Respondents dismiss the earlier administrative rulings as supposedly

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1 (Fed. Br. 12, 23; Sec. Pac. Br. 7, 16). Respondents imply the activity here was approved in *First Nat'l Bank* v. *City of Hartford*, 273 U.S. 548, 560 (1927). That case, a tax dispute, involved the sale of mortgages and not the public underwriting of securities reflecting an interest in the stream of income produced by those mortgages. In any event, that case was decided six years before the Glass-Steagall prohibitions were enacted.

2 *See* Pet. 13 & n.17. Security Pacific itself just recently underwrote $750 million in credit card receivables generated by VISA and MasterCard accounts. *See* "Security Does Card-Backed Issue," *American Banker*, Dec. 20, 1989 at 3.

relating to "third party" securities and not "own originated" loans. (Fed. Br. 20-23, Sec. Pac. Br. 16-17.) But, the ruling at issue is not limited to a bank's distribution of its own originated loans—it expressly encompasses any "lawfully acquired assets" (62a)—and the prior administrative rulings were not limited to "third-party" securities. For example, the Federal Reserve Board's recent *Citicorp* ruling specifically prohibited a bank affiliate from underwriting securities "representing interests in, or secured by, obligations *originated* or sponsored by" its related bank.[3] The ruling below reverses the prior consistent understanding of federal bank regulators that the bank activity permitted here is prohibited by Glass-Steagall.[4]

Respondents are equally incorrect in seeking to explain away the direct conflict between the holding below and the

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3 *Citicorp*, 73 Fed. Res. Bull. 473, 507 (1987), *aff'd sub nom.*, *SIA* v. *Board of Governors*, 839 F.2d 47 (2d Cir.), *cert. denied*, 108 S. Ct. 2830 (1988) (emphasis supplied). The Comptroller's earlier rulings similarly encompassed a bank's sale of its own assets. *See Investment Securities Regulation*, [1978-79 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,082 (Dec. 12, 1977).

Respondents similarly misconstrue specific legislation addressed to mortgage-backed securities as supposedly relating only to securities "issued by others." (Fed. Br. n.8.) The Secondary Mortgage Market Enhancement Act of 1984 ("SMMEA") is not so limited in its definition of a "mortgage related security." 15 U.S.C. § 78(c)(41). Moreover, Senator Proxmire, a major *proponent* of expanded bank securities powers, commenting on other pending bank powers legislation in 1984, left no doubt that banks could not underwrite even their "own originated" loans:

> While banks can issue mortgage-backed securities as originating mortgage lenders, they are precluded by law from selling them to the ultimate investor.

S. Rep. No. 560, 98th Cong., 2d Sess. 97 (1984) (emphasis supplied).

4 Respondents have no explanation for the anomalous result produced by the now conflicting interpretations of the Federal Reserve Board and the Comptroller. (Pet. 14-15, 21.) Bank *affiliates* subject to Federal Reserve Board regulation are severely restricted in underwriting securities backed by own-originated assets, whereas *banks* regulated by the Comptroller may now conduct such underwriting without limit—turning upside down Congress' intent to restrict banks more severely than affiliates in their securities activities. *See Board of Governors* v. *Investment Co. Institute*, 450 U.S. 46, 60 (1981).

decisions of this Court in *ICI* v. *Camp*, 401 U.S. 617 (1971) ("*ICI*") and *SIA* v. *Board of Governors*, 468 U.S. 137 (1984) ("*SIA*") (Pet. 15-16). Respondents claim *ICI* is inconsistent only if the "role of the bank" is "ignore[d]." (Sec. Pac. Br. 11.) That is not so. The role of the bank both here and in *ICI* is that of an underwriter offering securities to the public. In *ICI*, involving bank distribution of shares in a common trust fund, the Court held this "role" prohibited by Glass-Steagall even though the bank had authority to buy and sell stock for its customers and to pool trust assets. The rationale below would hold that Glass-Steagall could not prohibit the activity at issue in *ICI*, because banks may buy and sell the underlying assets for their customers.

Respondents go farther in arguing that *SIA* accepted the view that anything within the "business of banking" is not prohibited by Glass-Steagall. (Fed. Br. 13-14; Sec. Pac. Br. 9.) It did not. *SIA* involved notes ("commercial paper") that banks are expressly authorized to buy and sell. Notwithstanding this authority, the Court held Glass-Steagall did apply and banks were prohibited from underwriting the notes to the public. 468 U.S. at 157-58. The court below says that holding was wrong; if a bank has the power to sell an asset, in the Second Circuit's view, Glass-Steagall cannot restrict the means of that sale—even if it constitutes a public "underwriting."[5] The decision below repudiates the Court's decisions in both *ICI* and *SIA*.

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5 Security Pacific's claim that the ruling below "did not authorize 'underwriting' " (Sec. Pac. Br. 15-16) again bears no relation to the ruling. The Second Circuit found it "unnecessary" to reach the question, having found the activity within the "business of banking." (37a.) Moreover, the claim that the bank's public distribution of the securities is not "underwriting" rests upon the specious argument that the bank is not selling any third-party obligation, in that the securities represent the bank's *own* assets. To the contrary, the securities represent an obligation of the borrowers on the underlying loans, not an obligation of the bank. The prospectus expressly disavows any obligation of the bank for payments due on the securities. (58a.) It is a gross mischaracterization to imply no underwriting of "third party" securities was authorized.

CONCLUSION

For the foregoing reasons and the reasons set forth in the SIA's Petition, the requested Writ of Certiorari should issue.

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Respectfully submitted,

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